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HOW TO ANALYZE SEASONED RMBS POOLS IN THIS ENVIRONMENT?

They used to be golden! Few pools warranted lower credit enhancements than seasoned RMBS pools. Seasoning credits were applied for two reasons. Home prices used to appreciate substantially as loans aged, resulting in considerably lower loan-to-value (LTV) ratios, a primary driver for credit defaults. Second, since a borrower had already demonstrated a strong willingness and ability to pay, some of the underwriting characteristics, such as the level of documentation (doc) at origination, became less relevant, hence the associated default penalty factors would be reduced, and as such credit enhancements were lowered.

Times are different. What has happened in recent years is the opposite. Instead of home price appreciation, the housing market has collapsed. LTVs have escalated as pools aged, frequently reaching 125% and above. In addition, poor performance, as reflected in high delinquency rates, has eliminated any possibility to give credit to seasoned pools. Not only have the stated doc loans failed miserably, full doc performance hasn't held up either. In fact, many of the full docs were not underwritten in accordance with full doc quality – full income, asset, employment and mortgage verifications. Therefore, in recent seasoned pools, DBRS has regularly mapped full docs to lower categories in our default analysis. All else being equal, the resultant effect of less seasoned pool benefits, coupled with soaring LTVs, is naturally higher credit enhancement for seasoned pools.

Penalties regarding home price declines come in the form of lower property values and stressed LTVs. In stressing LTVs, DBRS first updates properties to their present value using Metropolitan Statistical Area (MSA) Case-Shiller home price indices. The values are then further stressed to the projected housing trough based on the Case-Shiller price projections for the next 12 months, with no credit given to any possible price appreciation in this period. For pools seasoned two to three years on average, containing significant concentrations in California or Florida, stressed LTVs may reach well above 125%. In addition to default frequencies, these stressed LTVs also have a considerable impact to loss severities in seasoned pools.

Modification is another key factor in evaluating seasoned pools. Many so-called current loans have been delinquent in the past but were subsequently modified. Due to high recidivism rates across all sectors, DBRS reviews all modified loans in conjunction with modification dates and pay histories. To the extent that a modified "current" loan has not demonstrated a consistently improved payment pattern for a minimum of one year, DBRS will revert its status back to delinquent when assessing the default frequencies. For example, a loan that was modified five months ago and was 60 days delinquent before modification may be treated as 60 days delinquent in determining default frequencies.

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